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29 March 2018

NSW Government
Treasury
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****CONFIDENTIAL****

Submission re the NSW State Government's Point of Consumption Tax on wagering in NSW - Consultation Paper

Betfair Pty Limited (**Betfair**) welcomes the opportunity to contribute to the NSW Government's review of a potential Point of Consumption Tax (**PoCT**) on wagering in NSW, and the design and operation of any such tax if it was implemented.

The **Consultation Paper** issued by the NSW Government clearly indicates this government has taken the time to understand that Betfair runs a betting exchange which is quite distinct from all other forms of wagering and plays a unique role servicing winning customers, high value/low margin customers, as well as other Australian licensed wagering operators. The importance this has to the Australian wagering landscape, the revenues Australian racing and sports bodies receive in the form of product fees and the retention of winning customers on-shore cannot be underestimated.

[REDACTED]

1. Overview of Betfair

Betfair, a company incorporated in Australia, is a wholly owned subsidiary of Crown Resorts Limited and is the only Australian licensed wagering operator of a betting exchange. The Betfair betting exchange (owned by Paddy Power Betfair) is a global exchange that allows customers from all over the world to bet against each other. Betfair holds the licence to operate the Betfair betting exchange in Australia and manages and services Australian and New Zealand customers.

Betfair does not offer fixed odds bookmaker or totalisator products, but instead operates a betting exchange which is an online platform that enables customers to bet against each other on an event at a known price they set. It operates in a manner resembling a stock market, in that punters can either back (i.e. buy) or lay (i.e. sell) an outcome on a racing, sporting or other event. This unique offering means the Betfair betting interfaces (desktop and mobile) are a lot more complex to understand and use than traditional bookmaker digital offerings.

Betfair's business model is very different to that of fixed odds operators and totalisator operators. In particular:

- a) the betting exchange model generates revenue via commission charged on a customer's net winnings on a betting market. If a customer has a net loss on a betting market, they do not pay commission and Betfair does not earn any revenue. By contrast, fixed odds operators generate revenue when customers lose, and totalisator operators take a set percentage from the pool of all bets before distributing the remaining amount to winning customers;
- b) because Betfair does not hold the risk on customers' bets, it does not restrict the size of their bets (as many fixed odds operators do);
- c) when customers bet using the betting exchange they are betting at a known price. By contrast, when they bet into the totalisator pools the odds are not known at the time of bet placement; and
- d) because the betting exchange requires opposing bets that match, customers have the ability to trade, for example betting that an event will occur (a "back bet") at odds of \$4.00 and then "trading out" by betting that the event will not occur (a "lay bet") at odds of \$2.00. Many customers employ sophisticated, automated trading strategies with multiple back and lay bets on the same betting market, generating very high levels of turnover relative to their net customer winning position. This results in Betfair's 'revenue margin' (wagering revenue as a proportion of wagering turnover) being far lower than that of a fixed odds operator and totalisator operator. For example, a totalisator operates on margins of approximately 16%, fixed odds operator's margins are approximately 13%, while Betfair's margins are typically 3% on racing and 1% on sports.

In many cases where customers employ sophisticated algorithms and high-volume trading strategies, this margin can fall below 0.1%. However, Betfair accepts this activity as it is all incremental revenue to racing and sports that can't be generated through other wagering operators.

The combination of a complex betting interface, winning customers being welcome at Betfair, attractive and known odds, and the ability to trade at competitive pricing, attracts a niche of sophisticated, price sensitive customers to Betfair that cannot be serviced elsewhere other than by illegal off-shore wagering operators.

2. Wagering landscape in Australia

The Australian wagering landscape can broadly be split into four groups; TAB operators (totalisator and fixed odds), corporate bookmakers, on-course bookmakers and betting exchanges.

As Betfair is the only licensed betting exchange in Australia and provides a unique service to a unique set of sophisticated customers, the prices on the exchange are generally referred to as the truest price of an outcome likely to occur. In racing circles the exchange is often referred to as 'the market'.

Given this uniqueness, bookmakers taking risk (both on-course and fixed odds operators) all use Betfair prices as an input into the prices they are willing to offer customers. For example, going into the betting ring and looking at on-course bookmakers' stalls will show they all use Betfair.

Similarly, customers use Betfair (either directly or through price comparison sites such as dynamic odds or punters.com) to shop around for price.

This reliance on Betfair to inform price for both the buy (customer) and sell (the wagering operator), has shown that when Betfair is down (i.e. due to maintenance for example), then industry wide turnover is down. Consistent examples of when Betfair has had a planned or unplanned outage show that this effect is a 17% drop in total turnover excluding Betfair.

A vibrant betting exchange ensures a vibrant wagering ecosystem which benefits not only customers and other wagering operators, but most importantly benefits the racing and sports bodies that receive product fees and governments who receive taxes.

3. Betfair’s customers

Betfair’s customers are not typically recreational style ‘back bet’ punters and for that reason are generally not also customers of fixed odds or totalisator operators. The combination of winning customers being welcome at Betfair, attractive odds, ability to trade and competitive pricing attracts a niche of sophisticated, price sensitive customers to Betfair.

Betfair’s mission is to *Champion Winning*, which we aim to achieve by continuing to provide the unique value and services we currently offer, and by improving the wagering IQ of Australian and New Zealand customers, so they win against ‘rest of world’ customers. An inability to service these unique customers, will lead to leakage of their activity off-shore to illegal wagering operators.

4. Taxation and compliance landscape in Australia

Fees and taxes

Australia has one of the most heavily regulated taxation and compliance landscapes for wagering operators in the world.

Betfair pays on average 51% of its net wagering revenue in fees and taxes (product fees, GST and wagering taxes) increasing to 66% for South Australian residents, before any operating costs, including payroll taxes.

Figure 1: Fees and taxes (including POC) as a percentage of Betfair’s net wagering revenues:



Product fee models

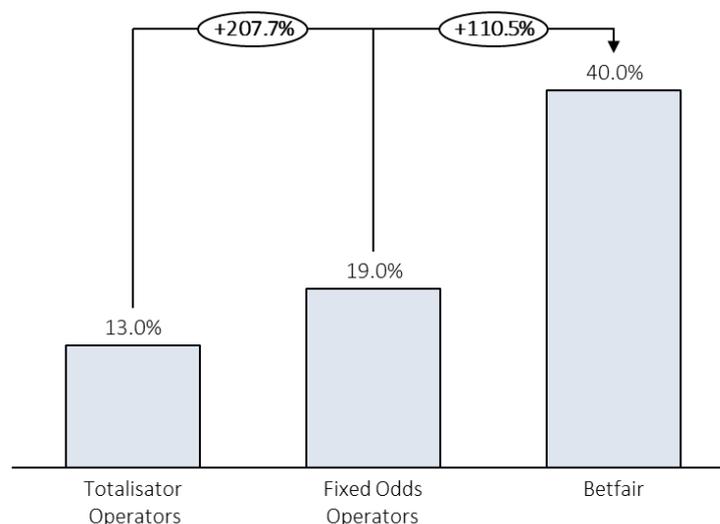
The use of turnover by some state racing bodies as a basis for product fees has favoured and currently favours totalisators and high margin fixed odds operators. By imposing turnover-based fees, the racing industry increases the relative price of wagering services offered by a betting exchange which operates on lower revenue margins in competition with high-margin totalisator and fixed odds operators.

Betfair is disproportionately affected by turnover-based product fee models because Betfair operates on the lowest gross margins or yields in the wagering market.

Some racing and all sports bodies in Australia recognise that Betfair is not a fixed odds or totalisator operator and have a policy that is suitable for a betting exchange (i.e. they charge a percentage of revenue). Other racing bodies yet to grasp the betting exchange model charge Betfair the same rate they charge a fixed odds or totalisator operator, which is at a percentage of turnover.

The result is that as a percentage of net wagering revenue, Betfair pays a much higher proportion of its net wagering revenues relative to what fixed odds and totalisator operators pay in relation to racing product fees. As shown in the graph below, Betfair pays over 200% more than totalisator operators and over 100% more than fixed odds operators in product fees to racing bodies in Australia as a percentage of net wagering revenue.

Figure 2: Estimated racing product fees as a percentage of net wagering revenue by wagering operator segment:



Notes:

- Totalisator operators – assumes yield of 16% and 2% of turnover product fee charge (average for racing)
- Fixed Odds operators – assumes yield of 13% and 2.5% of turnover product fee charge (average racing racing)
- Betfair – based on actual racing product fees for FY17

Betfair has been forced to increase its commission to customers in jurisdictions that adopt a turnover model to recover the high cost of product fees. A recent example of this is Racing NSW who increased their product fees in July 2017. Without a pricing increase this would have represented 64% of Betfair's net wagering revenue (before GST and wagering taxes), and therefore Betfair was forced to increase the commission charged to customers. As a result of this price increase, and to illustrate the impact an increased fee or tax can have on a low margin operator such as Betfair and its

customers, Racing NSW's growth year on year has now slowed. [REDACTED]

This clearly shows Betfair's customers are price sensitive and react to a price increase. Unfortunately, some of Betfair's most profitable winning customers have stopped betting on Racing NSW racing, moving their activity off-shore which has resulted in lost revenues for Betfair and Racing NSW.

5. Integrity Services

Betfair has invested significantly in technology and human capital to provide a range of valuable services and products to the racing industry, primarily in terms of its market-leading integrity systems. The Betfair Bet Monitor is a fully customisable web based application made available to our racing and sports partners which grants them oversight of the betting activity which is occurring on their product via the Betfair betting exchange in real time. It is currently used by all major racing and sporting bodies to assist in maintaining integrity in racing and sports.

Information provided in the tool includes account identification information, bet size, bet type and bet selection, giving our partners the ability to monitor in real time who is betting on their product. The information is also stored in the tool for up to 24 hours, allowing partners to access the information historically which can aide in ongoing inquiries and investigations.

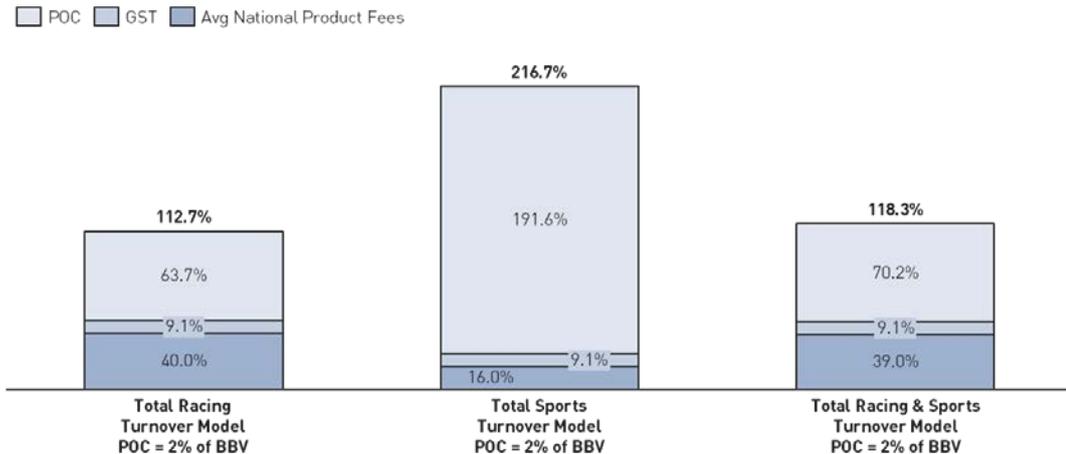
With Betfair being the only wagering operator who provides direct access to NSW racing and sports bodies of wagering information, these contributions are pivotal in maintaining public confidence in NSW racing and sports.

6. Impact of a PoCT on Betfair

The PoCT model introduced by South Australia (15% of net wagering revenue) has had a large impact on Betfair, increasing fees and taxes paid as a percentage of Betfair's net wagering revenue from 51% to 66%, leaving only 34% to operate the business and invest in infrastructure and innovation.

A turnover model has a far greater impact due to the low margin nature of Betfair. Essentially as evidenced by the graph below, a 2% of turnover model puts Betfair out of business. It would result in Betfair paying approximately 113% of the net wagering revenue it earns from racing in fees and taxes, and 217% of the net wagering revenue it earns from sports – on average almost 120% of its total business in fees and taxes.

Figure 3: Product Fees, GST and POC (at 2% of Turnover) as a percentage of Betfair's net wagering revenues:



Note:

- BBV = Back Bet Volume which is the total of all the back side of bets wagered through the betting exchange.

7. Response to questions posed in the Consultation Paper

1. Should NSW introduce a PoCT on wagering? If so, why? If not, why not?

Betfair accepts the NSW Government is likely to introduce a PoCT primarily due to what was outlined in the Consultation Paper: *“the change in the wagering landscape has led to a disconnect between the location of the wagering activity, the jurisdiction where the profits from the wagering are earned, and taxation revenue from wagering.”*

Betfair's preference has always been for a national approach to overcome the complex and fragmented state based regulatory environments. Given this is now an unlikely outcome, Betfair recommends that where possible, an approach that harmonises each state-based model is implemented, taking into consideration PoCT models from states that have sought consultation from stakeholders. That is, the model implemented in South Australia should not be considered given there was no consultation with any stakeholders (wagering operators, racing and sports bodies, punters, etc).

Any PoCT introduced in NSW should have regard to:

- the current level of fees and taxes already paid by Betfair as outlined in section 4, and the impact an additional tax will have not only on Betfair but the broader wagering ecosystem and the racing and sports bodies who receive product fees;
- setting a fair and equitable model that will encourage sustained, long-term growth;
- the uniqueness of Betfair; and
- the importance low margin operators play in servicing a niche segment of wagering customers in the national wagering landscape.

2. If NSW was to introduce a PoCT, which PoCT design elements should be harmonised across jurisdictions, and why?

As a national model is unlikely to be implemented, to avoid a multi-jurisdiction, differentiated PoCT model by state, Betfair supports most elements be harmonised. As stated in response

to question 1, harmonisation should not be linked to models where there was no consultation (e.g. South Australian model), nor any model that seeks to reflect the South Australian model (e.g. potentially the Western Australian model).

To date, Victoria is the only government that has actively engaged stakeholders in the design of its PoCT model, and we would encourage the NSW Government to consider the Victorian model to ensure a consistent approach is applied.

A consistent approach will not only benefit wagering operators and punters, it will benefit racing and sports bodies in each state as it will ensure there is no discrimination against any particular state due to a more or less favourable PoCT model.

A good precedent has already been set by the NSW Government in terms of a consistent approach when it moved to align pari-mutuel and fixed odds tax rates in NSW to Victoria. This alignment, when fully realised by 2019/20 will promote consistency and fairness across both states for racing and sports, as well as punters.

Betfair supports the following elements being harmonised across jurisdictions:

- a) The **same model** be used by each state. Betfair supports a **percentage of net wagering revenue as the preferred model**. With respect to net wagering revenue, the definition of net wagering revenue for each type of wagering operator needs to be clear and unambiguous ensuring a betting exchange is not included in the standard definition for fixed odds and totalisator wagering operators as was the case with the South Australian legislation.

- b) **Definition of net wagering revenue** for a betting exchange must be correctly defined as:

“net NSW wagering revenue” — the net State wagering revenue of a betting exchange operator for a financial year is the GST exclusive sum of all commission on winning bets received by the betting exchange operator from persons located in NSW.

- c) The **same PoCT rate be used by each state**. Betfair is supportive of an appropriate rate that is fair and equitable and will encourage sustained long-term growth across all wagering operators.

Betfair does not support a punitive fee as high as South Australia's (15% of net wagering revenue) or a turnover model that will make Betfair unviable. Betfair supports a sensible approach to the rate and recommends the NSW consider a rate that is inclusive of the GST paid and aligned to the Victorian model.

- d) The **customer location** must be the same across all state models to ensure wagering operators are not charged PoCT twice for the same bet.

Betfair's preferred position is to use the customer's registered residential address.

- e) **Administration** and lodgement of PoCT returns should be aligned to reduce the compliance, administration and cost imposed on wagering operators to lodge regular PoCT returns with each state.

Australian licensed wagering operators already lodge approximately 30 race fields/product fee returns on a monthly or quarterly basis to Australian racing and sports bodies.

3. Should a PoCT be levied on the operator's net wagering revenue (player loss) or on the operator's wagering turnover? Why?

Betfair, as a betting exchange, has neither player loss or turnover. As Betfair operates a betting exchange, customers bet against each other on an event at a known price they set, which means Betfair does not have any turnover or hold any risk.

Instead, Betfair charges a commission on the net customer winnings.

Some racing bodies charge Betfair on a turnover basis with the turnover metric either defined as Back Bet Volume (BBV) which is the back side of all the matched bets or Net Customer Winnings (NCW) which is the net winnings for a customer on a particular market. Neither are actually correct as Betfair does not take turnover.

Betfair recommends that for a betting exchange, PoCT is levied on the only possible metric, which is commission, as defined at Question 2 above.

From a broader wagering perspective, it's Betfair's view that net wagering revenue (or player loss) is the correct metric to use as it is the real measure of an operator's activity. Additionally, it is the most appropriate measure for alignment. That is, it's in every wagering operators interests to maximise revenues in order to maximise profits. Linking a levy to revenue ensures alignment to maximise returns.

4. Should all forms of wagers (online and terrestrial) be captured by a PoCT at a common tax rate?

Any PoCT implemented should apply to all wagers equally if as stated in the Consultation Paper, it is to address the disconnect between the location of the wagering activity, the jurisdiction where the profits from the wagering are earned, and taxation revenue from wagering.

5. Should a common PoCT rate apply to all wagering types (fixed odds, totalisator, betting exchange, etc)?

While Betfair would advocate for a different rate for a betting exchange as the wagering type is distinctly different to that of bookmakers, if an appropriate percentage of net wagering revenue is recommended that is fair and equitable, then Betfair supports treating all wagering types equally.

If the NSW Government was open to harmonise a PoCT rate with other states, and assuming they looked towards states that have carried out extensive consultation such as Victoria, then it would be appropriate to apply a common rate to all wagering types.

If, however a turnover model was recommended which is extremely punitive to a high volume/low margin business such as Betfair (as indicated in section 6), then the fair and equitable approach would be to include a revenue percentage cap to ensure Betfair would not be disadvantaged compared to high margin wagering operators.

6. Should a customer's location be defined through their usual residential address for the purpose of a PoCT, or should it be based on where the bet was made? How should this be verified and updated?

The most appropriate and logical approach is to use the registered residential address of the individual. This would align to the model in South Australia, and ensure wagering operators are not taxed twice for the same bet.

7. What should the PoCT rate/s for NSW be? For which reasons?

The recommended rate needs to be cognisant of a number of issues:

- a) The already heavily taxed regime Australian wagering operators must comply with. Betfair pays 51% of its net wagering revenues in product fees, GST, and wagering taxes, which increases to 66% for South Australian residents.
- b) The 15% revenue rate used by the South Australian government was taken from the UK model which was introduced to levy off-shore to the UK wagering operators in relation to bets taken from UK residents. The rate was used without the context of the minimal fees and taxes these wagering operators pay as compared to the already heavy fee and tax regime in Australia before POC.
- c) Is set at a rate that ensures NSW residents can continue to find value and bet with their wagering operator of choice.
- d) Is not set too high as to deter NSW residents from betting with legal on-shore wagering operators, and instead turning to illegal off-shore wagering operators who can provide far better value as they do not pay any product fees or taxes in Australia.
- e) Is not set too high as to negatively impact the product fees paid to NSW racing and sports bodies who are heavily reliant on this revenue stream to fund their industries, including integrity.
- f) Allows the wagering industry to continue to grow and support not only racing and sports bodies but provide job retention for current employees within both the racing/sports and wagering industries, and be able to attract future talent to ensure continued innovation.
- g) Allows wagering operators to continue to invest in integrity and AML management.
- h) Allows wagering operators to continue to invest in and contribute to consumer protection.

8. Should there be a tax-free threshold? If so, at what level? Should on-course bookmakers be exempt from a PoCT?

Betfair understands and supports the role on-course bookmakers play that allows punters to bet with an alternative to the TAB on-course, while at the same time providing the vibrant on-course punting experience.

Betfair has a long history of working closely with on-course bookmakers with most being VIP customers of Betfair [REDACTED]

[REDACTED] Betfair's betting exchange also plays an important role in providing on-course bookmakers with the ability to 'lay off' their liabilities with Betfair, ensuring they can take almost any bet from a punter on-course.

In response to the 15% of net wagering revenue PoCT introduced in South Australia, Betfair made the tough decision to remove the discount rate for all South Australian residents including on-course bookmakers. Betfair would be incredibly disappointed if it was forced to do the same in NSW. This would have a detrimental impact on the livelihoods of NSW on-course bookmakers and lead to the demise of the vibrant on-course experience.

Betfair would support a tax-free threshold similar to the threshold Racing NSW has in their Race Fields Information Approval (\$5m turnover) which was included to support on-course bookmakers.

Betfair urges the NSW Government to consider the potential wider impacts to on-course bookmakers if a punitive rate of PoCT is recommended.

9. Estimates of the take-up of illegal offshore wagering are uncertain. Stakeholders are encouraged to provide any relevant information or evidence of on the sensitivity of punters to changes in odds and shifting to offshore operators.

Until Monday 12 March 2018, Pinnacle, an illegal off-shore sports wagering operator, continued to breach the *Interactive Gambling Act 2001* (Cth) and take bets from Australian customers. On Monday 12 March 2018, Pinnacle advised their Australian customers their accounts were being closed and they could no longer accept bets from Australian customers. Pinnacle is renowned as a smart, low margin wagering operator that provided customers with the ability to get good odds at the volumes required.

A simple search of “Pinnacle” on Twitter on or around 12 March 2018 will show numerous threads from disappointed customers that can no longer bet with Pinnacle, which highlights not only the prevalence of Australian customers betting with illegal off-shore wagering operators, but also the need for legal on-shore options for price sensitive customers.

Australian customers can still continue to bet with Pinnacle by using a VPN, and will do this if value cannot be found amongst the Australian wagering market due to the high rates of fees and taxes paid by wagering operators in Australia.

Citibet, an illegal betting exchange in the Philippines, continues to operate allowing Australian customers to bet on global racing, including Australian racing.

[REDACTED]

10. What has been the experience of operators in complying with South Australia’s PoCT administration procedures?

The level of administration is low with a simple monthly return and payment.

If the NSW Government introduces a PoCT, Betfair would encourage an adoption of a similar process, but consider a quarterly or bi-annual return and payment to reduce the burden of submitting multi-jurisdiction PoCT returns and payments on top of the already burdensome racing/product fee returns and payments cycle.

11. What are the practical issues and challenges for stakeholders in implementing a PoCT, and what would an appropriate implementation timeframe be in NSW?

Betfair would seek an implementation plan of up to 12 months to enable appropriate consultation with the NSW Government to review the legislation and guidelines and ensure its understood and applied correctly.

12. Is there a preference for coordinated PoCT collection by a single state or revenue office?

Betfair was supportive of a national PoCT model which would ensure a harmonised approach across Australian jurisdictions. Given several states have announced or implemented PoCT regimes that are different, it is not practical or recommended for collection to be administered by a single state or revenue office.

8. Summary

The NSW Government must conduct thorough research and analysis to fully understand the impact of a heavily taxed environment which will result from the imposition of a PoCT. There will be leakage off-shore and a number of unintended consequences including:

- lower returns to customers;
- reduced integrity oversight and funding leading to a complete blind spot on integrity;
- reduced consumer protection;
- reduced taxation revenues for Federal and State governments;
- reduced product fee, sponsorship and media revenues for racing and sports;
- the demise of the on-course bookmaker and the vibrant on-course racing experience; and
- lack of competition in the wagering industry resulting in reduced consumer choice and service.

Betfair understands the desire of the NSW Government to introduce a PoCT, however urges that a fair and equitable revenue based PoCT mode (not a turnover based model that would make Betfair unviable) be recommended. A revenue based PoCT model at an appropriate rate will ensure there is:

- opportunity for continued growth and job retention for employees;
- ability to retain and gain new customers through competitive pricing;
- continued contribution to integrity and AML management;
- continued contribution to consumer protection; and
- continued support of racing and sports bodies through product fees, integrity support and growth initiatives.

We request that this submission be kept confidential and not published in the public domain. We would welcome the opportunity to meet with you to elaborate on the matters we have raised above. If you are available for such a meeting, or have any questions about the above, please contact me.

Regards,



Tim Moore-Barton
Chief Executive